

May 24, 2019

Via ECFS

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th St. SW
Washington, DC 20445

Re: *Promoting Telehealth and Telemedicine in Rural America, WC Docket No. 17-310*

Dear Ms. Dortch:

GCI Communication Corp. (“GCI”) submits the attached paper, “The Role of Competitive Bidding Based Prices in Determining the Rural Rate,” which was prepared by Dr. Agustin Ros and Mr. William Zarakas of The Brattle Group. GCI submits this paper in support of both its Application for Review¹ and its comments in the pending Notice of Proposed Rulemaking addressing potential changes in the rules implementing the statutory Rural Healthcare Telecommunications Program.² The paper notes that the rates for the services provided to rural healthcare providers have been substantially deregulated. To the extent a backstop to competitive bidding is needed, it suggests reliance on market data, including element-by-element comparisons where end-to-end comparisons are not available or appropriate. It also explains that from an economic perspective there is no reason why the sum of the component rates would not be reasonable. As Dr. Ros and Mr. Zarakas observe (at 4), “either competition or regulation provides a check on the prices for termination and middle mile services,” and thus, “the reasonableness of prices for an end-to-end service can be approximated by the reasonableness of prices of its component parts.”

The Brattle paper also provides an economic critique of the use of fully distributed cost-based studies to set rates for carriers operating in competitive markets. They conclude (at 10), “calculations of cost-based rates do not reflect market prices, regardless of how common costs are allocated,” and “a requirement to provide cost-based rate calculations is a step much

¹ Application for Review of GCI Communication Corp., WC Docket No. 17-310 (filed Nov. 9, 2018) (“GCI Application for Review”).

² Reply Comments of GCi Communication Corp., WC Docket No. 17-310 (filed Feb. 19, 2019) (“GCI Reply Comments”).

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closer to an *ex ante* regulatory regime that the Commission no longer applies to non-dominant carriers and providers of the majority of business data service.”

Please contact me if you have any questions.

Sincerely,



John T. Nakahata

Counsel to GCI Communication Corp.

cc: Giulia McHenry
Trent Harkrader
Elizabeth Drogula
Ryan Palmer
Johnnay Schreiber
Shane Taylor
Tracy Waldon

Attachment

In the Matter of
Promoting Telehealth and
Telemedicine in Rural America

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WC Docket No. 17-130

The Role of Competitive Bidding Based Prices in Determining the Rural Rate

William Zarakas and Agustin J. Ros
Principals, The Brattle Group

May 24, 2019

I. Introduction and Summary

Counsel for GCI Communication Corp. (“GCI”) asked us to opine on the appropriate approach for the Commission to apply in determining the rural rate under 47 CFR § 54.607(a) and (b). Counsel also requested that we provide our opinion as to the appropriateness of the use of a benchmark discount contemplated under the FCC’s Notice of Proposed Rulemaking and Order (“NPRM”) WC Docket No. 17-310 in the Matter of Promoting Telehealth in Rural America.

Both of these issues are closely related in that they are motivated by concerns that the bids made by telecommunications providers in response to requests by rural healthcare providers (and posted and processed by USAC) are not sufficiently competitive and may reflect unreasonable market power. Section 54.607 and the proposed benchmark discount contemplated in the NPRM provide regulatory backstops, generally aligned with the historical regulation of rate of return local exchange carriers. However, the FCC and the individual states have substantially deregulated many of these services, including all interexchange services and most business data services, based on the prevalence of actual or potential competition to mitigate the exercise of unreasonable market power.

While we are sympathetic to the spirit of the regulatory backstop in Section 54.607, its implementation is increasingly challenging, and will likely misrepresent market prices. Section 54.607 and the Commission’s NPRM are aimed at ensuring that the prices paid by rural healthcare providers for broadband services are reflective of the prices paid for like services in competitive markets. The market for broadband services has evolved considerably since the issuance of Section 54.607, and broadband products have become more nuanced and differentiated. This makes “apples to apples” pricing comparisons a challenging exercise. Even in cases in which comparisons are more direct, pricing data are typically not publicly available, even in areas subject to robust competition. Tariffing is no longer required, or even permitted, for many of these broadband services. The difficulty of “apples to apples” pricing comparisons is still more pronounced in rural areas—the target audience for the Commission’s RHC program—because there are few users of similar services. When they are present, the services provided are frequently at different

bandwidths and reliability levels, and are provided under different terms and contractual arrangements than what an RHC customer requires. Thus, it is not uncommon for winning telecom carriers to be unable to provide the Commission with market comparable data at a sufficient level to meet the specifications of Section 54.607, particularly with regard to an end-to-end circuit.

The final fallback in the Commission's regulatory backstop—calculating cost-based rates—may be arithmetically simpler than garnering market comparables, but it will almost certainly lead to inaccurate results. Even though such a cost of service methodology has been a staple of common carrier monopoly utility regulation over the years, it is well understood that calculating the costs of a single product for a single customer class (within a larger multi-product/multi-customer company), or a subset of that class, depends on numerous assumptions, notably concerning the allocation of sizable common network costs. Thus, while the Commission may be able to “check the box” by having a cost of service study in hand, it would not be informative of competitive market prices.

The Commission should consider two types of pricing data that may fill this gap. First, the competitive bidding process required under 47 USC § 254 will produce a range of market-based prices for services in various rural areas. Pricing data for similarly situated services, albeit not from the same geography, will likely be forthcoming from these data, and can be used as proxies of market prices. Second, the market prices and/or tariffed rates for components making up an end-to-end service can be used to build up an end-to-end price comparison. Both of these methods will produce pricing points that are more reflective of market realities than would be a calculation of the fully distributed cost for a subject service. In our view, these market-based pricing data are preferential to information conveyed via a cost study when setting a rural rate.

Using market-based prices also avoids the pitfalls of a benchmarking approach. The premise behind the benchmark approach is that outlier service prices may be indicative of bad acts; i.e., waste, fraud and abuse. While some price outlier may indeed fit this bill, it is not a foregone conclusion that such a targeting methodology will accomplish the Commission's goals. Many price observations will fall into the outlier category because they reflect services to locations in the difficult to serve, high cost areas that the Commission's RHC program is designed to support. In these circumstances, subjecting the outliers to cost-based ratemaking will do little to address concerns about waste, fraud and abuse. Such concern could more directly be addressed by making the soliciting party (the rural healthcare provider) more financially interested in bidding outcomes by increasing the percentage of their contribution to monthly telecom service charges, while keeping in mind the statutory purpose of rate comparability with urban areas.

II. Considerations of Market Comparable Data

Competitive bids accurately reflect the prices that telecommunications providers are willing to charge for a clearly defined telecommunications service (e.g., bandwidth and location) at a specific point in time. As such, competitive bids are superior to other options to estimate market prices, such as collecting and comparing prices paid for similar services—mainly because such transactions

are typically not similarly situated in important dimensions. Telecommunications services are specified based on a range of criteria, including bandwidth, technology level of service (e.g., dedicated service vs. best effort), location(s) and volume, and are also subject to contract terms and conditions. Thus, compiled pricing information on potentially similar, but not precisely equivalent (in terms of service criteria, location and even time frame), transactions is unlikely to accurately reflect the market price of the specific telecommunications service under study.

Rate or price data may be compiled for various regulated industries, such as electric utilities, because, in most circumstances, utilities are required to file tariffs or other rate related information. However, even there, pricing information for services that are considered competitive is not always forthcoming. For example, the rates charged by utilities to large industrial customers are frequently set on an individual case basis (ICB) and, while available to regulators, are treated as confidential and not made available to the public. Prices for telecommunications services are largely de-tariffed, and related conditions (e.g., terms, volumes and discounts) are treated confidentially, and thus are not available outside of the parties to the contract. Thus, the scope of available market comparable pricing data tends to be sparse.

47 CFR § 54.607 provides two options for telecommunications carriers and rural healthcare providers to apply market comparable pricing data in determining the rural rate. As shown below, market pricing data can be compiled from either the telecommunications carriers' own internal information or from data made public by other carriers.

- (a) The average of the rates actually being charged to commercial customers . . . for identical or similar services provided by the telecommunications carrier providing the service in the rural area in which the health care provider is located.
- (b) The average of the tariffed and other publicly available rates . . . charged for the same or similar services in that rural area over the same distance as the eligible service by other carriers.

In practice, though, these options are more difficult for telecommunications carriers serving rural areas to fulfil than may initially meet the eye. There are typically few large customers in rural areas, thus finding a similarly situated commercial customer in the rural area in which the healthcare provider is located is frequently not possible. Furthermore, even when a similarly situated commercial customer is present in the same rural area, they may not be purchasing an identical or similar service to what the healthcare provider is purchasing. In addition, for the reasons discussed above, collecting pricing data from other carriers in the same or even other rural areas is typically not feasible because pricing data is closely guarded and not publicly available. The challenges associated with collecting market comparable data led the Commission to issue its Data Collection Order in order for Staff to be able to complete analysis in its investigation of Business Data Services ("BDS"). Compiling these data was a lengthy and time-consuming process

that required some carriers “to pull data manually from numerous billing and data systems, diverting limited time and resources from other critical projects.”¹

This problem may be overcome in many instances by considering the price comparability of the elements or components that make up the end-to-end service under study, an approach not allowed under the Commission’s current interpretation of its requirements.² It is indisputable that a comparison of end-to-end prices is the ideal basis for comparison where available, but it is frequently infeasible to conduct genuine “apples-to-apples” comparisons in many situations. For these, assessing the comparability of the elements or components provides a suitable, practical, and available alternative that provides accurate representations of the prices for end-to-end services.

The components or network elements that make up the end-to-end services provided to rural healthcare providers consist of the channel terminations (which connect the ultimate service location to the providing carrier’s facilities) and middle mile (*i.e.*, long distance) transport. Both of these components are standalone telecommunications services in their own right. Furthermore, they can be procured from different carriers (e.g., channel terminations can be acquired by a local exchange carrier while transport can be acquired from an interexchange or other carrier). The Commission found middle mile transport and certain geographic markets for channel termination to be competitive services; *i.e.*, the prices for such are disciplined by the market, and not subject to regulation. And in those geographic markets where the Commission has found limited competition to provide channel terminations, it has required tariffed-based price regulation. Thus, either competition or regulation provides a check on the prices for channel termination and middle mile services. Following from this, the reasonableness of prices for an end-to-end service can be approximated by the reasonableness of prices of its component parts.³ That is, because there is no

¹ *Business Data Services in an Internet Protocol Environment, Report & Order*, 32 FCC Rcd. 3459, 3557 ¶ 104 (2017)

² That is, as articulated in a recent Public Notice, eligible prices are currently limited to comparable end-to-end services, not rates for elements or components that make up the overall end-to-end service. *The Wireline Competition Bureau Provides Guidance Regarding the Commission’s Rules for Determining Rural Rates in the Rural Health Care Telecommunications Program, Public Notice*, DA No. 19-92, WC Docket No. 02-60 (rel. Feb. 15, 2019). GCI has filed Petition for Reconsideration of that Public Notice, in part arguing that the exclusion element-by-element comparisons is irrational. Petition for Reconsideration of GCI Communication Corp., WC Docket Nos. 02-60 & 17-130 (filed Mar. 18, 2019) (“GCI Petition for Reconsideration”). GCI has pending before the Commission an Application Review that raises a similar objection to the Wireline Competition Bureau’s refusal to consider element-by-element comparisons when considering whether to set GCI’s rural rates under 47 C.F.R. § 54.607(b). Application for Review of GCI Communication Corp., WC Docket No. 17-310 (filed Nov. 9, 2018) (“GCI Application for Review”).

³ In other words, the prices for channel termination and middle mile transport can be used to impute a price ceiling for the end-to-end broadband service. If the prices for the wholesale inputs are found to be just and reasonable, so too will be the imputed price for the end-to-end service.

exercise of market power for any element of service, there is subsequently no exercise of market power over the circuit as a whole. For rural Alaska, this means that prices can be reviewed and compared separately for, for example, channel terminations, satellite-based middle mile transport, and terrestrial-based middle mile transport.⁴

Adding market comparable prices and tariffed rates for service components (channel terminations and middle mile transport) to meet the testing requirements of 47 CFR § 54.607 (a) and (b) expands the possibilities that price and rate observations can be effectively used as a basis for determining the applicable rural rates. Absent this, Section 54.607 then defaults to a third regulatory backstop test, which we find to be problematic:

- (b) . . . If there are no tariffed or publicly available rates for such services in that rural area, or if the carrier reasonably determines that this method for calculating the rural rate is unfair, then the carrier shall submit for . . . the Commission's approval, for interstate rates, a cost-based rate for the provision of the service in the most economically efficient, reasonably available manner.

The Commission raised the possibility of incorporating cost information as the basis for setting rural rates in its Notice of Proposed Rulemaking and Order in WC Docket No. 17-310. In the NPRM, the Commission queried whether it should “limit the acceptable rural rate associated with the funding request to those specific costs plus a reasonable rate of return.”⁵ Providing such cost-based information would require the affected carriers to conduct a cost study which, based on past experience, typically involves a fully distributed costing methodology. We find that a cost-based backstop for determining the rural rate provides false assurance at best. In addition, requiring participating carriers to conduct cost of service analyses may produce unintended consequences, providing disincentives to carriers from undertaking the investment to serve rural health care providers, reducing competitive alternatives, increasing the costs of the ultimate service provided to rural healthcare providers, and increasing costs to the Universal Service Fund. Requiring that carriers complete cost of service studies is also costly in terms of time and resources and, because pricing will then depend upon regulatory review and approval, introduces additional uncertainty into carrier planning and marketing efforts.

III. Fully Distributed Costs

Rate or price methodologies based on fully distributed cost (“FDC”) are a means of assigning all costs to a service and/or customer class, thereby ensuring that all costs are spoken for and that

⁴ It is also reasonable to consider different (and different sized) geographic markets in conducting price comparability analysis. Specifically, (local) channel terminations are sold in a smaller (sized) geographic market than are middle mile (interexchange) services.

⁵ NPRM at 49.

collected revenues will (at least theoretically) cover costs.⁶ However, it is widely understood that prices set in competitive markets are not based on FDC methodologies. In competitive markets, other factors, notably demands by customer segments for the myriad products and services offered, are factored into pricing decisions more thoroughly than are allocations of common costs.⁷ FDC was used as a mechanism in monopoly service conditions, but imperfectly even then. There was little or no expectation that rates based on FDC actually mimicked the prices that would have existed in competitive markets. In our view, using FDC as a backstop to determine rural rates will do little to inform the Commission's queries concerning market prices.

A. The Common Cost Allocation Problem

Utilities and telecommunications carriers are “multi-product” firms. That is, they offer a range of services to a range of customer segments through a network, much of which is “common.”⁸ In the case of service provided to rural healthcare providers over a middle mile network that also serves non-healthcare commercial, governmental and educational enterprises, as well as mass market fixed and mobile broadband customers, the entire cost of the middle mile network is likely to be common to all services provided over that network. Accordingly, in accounting terms, a significant percentage of the infrastructure operated by a network industry falls into this common category. For a middle mile network, all of the infrastructure may be accounted for as common network costs.

Regulators developed FDC pricing in order to allocate shared and common costs where competition was lacking for the (rate regulated) service. FDC begins by classifying the different components of the revenue requirement into different types of costs—such as costs that vary with the number of customers, costs that vary with the usage of the service, and costs that vary with the capacity imposed upon the network. Importantly, it continues by then developing allocators whose primary purpose is to assign the costs of the different plant and operating expenses to the customer classes and to the different services based upon the relative amount of, for example, usage that each class or service represents. No account is taken of the value that each customer class obtains from the service nor any other demand consideration that normally is used in competitive markets to recover shared and common costs.

Parsing out the common costs is thus a very important determinant of the rates ultimately calculated under an FDC methodology. In practice, these allocations are based more on arbitrary accounting convention than on clear indications of cost causation. For example, it is not possible

⁶ This is a very brief and simplified description of the regulatory process that is applied to monopoly providers.

⁷ This is not to say that a firm in a competitive environment is unconcerned about recovering all of its costs and making a profit. However, these firms do not use FDC methodologies to do so.

⁸ The prevalence of common infrastructure and the efficiency benefits associated with reaching scale economies was one of the main reasons why infrastructure providers, such as electric distribution utilities and landline telephone companies, were given monopoly status and franchise protection.

directly to assign the cost of constructing and operating a given middle mile segment to only one of the services transiting that segment on the basis that that service, and only that service, caused the construction and operation of that segment. Accordingly, from an economic perspective, such allocation untethered from demand is largely arbitrary, and lacks a solid and accepted foundation in economic theory. Thus, rates based on FDC therefore reflect costs to some degree, but the numerous assumptions concerning allocation of common costs involved makes it so these rates do not necessarily reflect cost causation.

Despite its use in regulatory applications, it is well understood that rates based on FDC are inaccurate. Regulatory economist Alfred E. Kahn, who led the deregulation of the airline industry in the 1970s and also served as the Chair of the New York Public Service Commission, noted that: “[t]rying to allocate fixed costs that are common to several services in an efficient and fair manner is like trying to find a black cat in a dark room where there is no cat.”⁹

Setting rates based on FDC was, and for regulated utilities still is, a convenient methodology to distribute costs. But it provides false assurance that the resulting rates mimic the prices that would be observed in competitive markets. From a practical standpoint, FDC based ratemaking methodologies worked “fine” (putting aside concerns by customer groups that resulting rates may not be truly cost based) within a monopoly environment. However, telecommunications markets have evolved from monopoly to competitive, and FDC cannot be used as a proxy for prices that would evolve in a competitive market.

The inapplicability and erroneous nature of the use of FDC pricing to attempt to set efficient prices—and in the early days of telecommunications to attempt to set an efficient price floor for the incumbent’s services that were being increasingly exposed to incipient competition—has been highlighted in the economics literature. In his book *Superfairness*, William J. Baumol states: “No form of cost allocation can pretend to be compatible, generally, with efficiency in resource allocation, no matter how sophisticated its derivation.”¹⁰

Mixing the basis for setting prices also exposes carriers to the risk of cost under-recovery. Under the Commission’s rules, some carriers may find themselves providing rate regulated services (with rates set based on FDC) as well as services under which prices are set based on competitive conditions, where this was not the case in the recent past. This introduces additional uncertainty and may adversely affect investment decisions.

B. Customer Demand

FDC-based ratemaking methodologies use only cost information in establishing prices, and do not utilize or take into account the demand characteristics of the various customer segments or classes that can materially influence the *opportunity cost* of service provision. This is in stark contrast to

⁹ Letter from Professor Richard Schmalensee to Rep. Dingell, dated March 14, 1994.

¹⁰ William J. Baumol, *Superfairness*, MIT Press, Cambridge 1987, p. 146.

the way that prices are set in competitive network industries, such as in the airline, banking, ride sharing services, and broadband industries. Economic theory teaches that the competitive market prices for particular customer segments in network industries must account for both marginal production costs and the opportunity costs associated with a sale in that customer segment. In other words, efficient market prices in competitive network industries cannot be determined without reference to demand information. This is the main criticism that many economists have voiced when attempting to use FDC to provide efficient market signals to participants. It is highly unlikely that the resulting FDC-based rates will be “efficient” from an economic perspective; that is, they will not send appropriate pricing signals to the marketplace.

Ratemaking based on FDC is a viable methodology for industries which operate in monopoly markets; that is, markets in which competition is largely or entirely absent and in which the monopolist serves most if not all customers. These tend to be mainly utility markets: electricity distribution and transmission, natural gas pipelines and distribution, and water distribution. Use of an FDC methodology provides some assurance that the utility will recover the costs that regulators deem necessary for it to remain a financially viable enterprise. However, even here, customer groups debate whether common network costs are appropriately allocated, as slight changes in allocation percentages may have a disproportionate effect on specific rates. Thus, while FDC provides a mechanism through which total costs can be recovered in a methodical way, individual rates for a service and for a specific customer class may not be an accurate representation of the value customers receive and may not reflect the price that would have been charged for the service in a competitive market.

C. Backward Looking

An additional problem and distortionary effect of FDC pricing is that it is backward looking—because its purpose is to facilitate recovery of the prudently incurred costs of utility production. Market prices, on the other hand, are inherently forward looking which send efficient price signals to consumers and producers and provide them with the relevant economic tradeoffs and the true economic opportunity costs that their decisions impose on society. Thus, the use of FDC to set reasonable rural healthcare rates is economically incorrect and incompatible with efficient pricing.

Section 54.607 recognizes the inadequacies of using backward looking costs as a proxy for market prices in stating that the cost-based rate should be “for the provision of the service in the most economically efficient, reasonably available manner,”¹¹ and by providing two preferred methods of establishing the rural rate before turning to a cost study. Developing hypothetical rates that reflect the most economically efficient provision of service would require an effort akin to the modeling total service and total element long run incremental costs (“TSLRIC” and “TELRIC”, respectively) during the implementation of the Telecommunications Act of 1996. But even setting rates based on those methodologies is hypothetical and not truly reflective of market prices. Also,

¹¹ § 54.607 Determining the rural rate (b).

experience at the federal and state levels revealed that the regulatory and transactions costs associated with developing and litigating these models were enormous.

Ethernet broadband is becoming the preferred service sought by users, including rural healthcare providers. Competitive bidding will provide more insight into the appropriate pricing for these services than will costing methodologies.

D. Broadband Markets

Telecommunications carriers are prime examples of firms that use a common network to provide a range of products to a variety of different customer classes. Like utilities, telecommunications carriers were regulated under a rate of return regime in which rates were set using a cost of service/fully distributed cost methodology. Such a rate methodology was discontinued for many carriers and services as the telecommunications became more competitive—in large part because it became increasingly difficult to set FDC based rates on the one hand and realize prices determined by market forces on the other.

GCI's TERRA network provides a good example. The network provides services to a variety of customer segments, including rural healthcare providers, schools and libraries, retail mass market, and enterprise customers, each of which procure from a range of telecommunications services, ranging from voice to broadband. In addition, wholesale customers lease capacity on portions of the network. The incremental costs that can be clearly assigned to a specific customer or customer class for a specific end-to-end telecommunications service likely constitute a small proportion of the total revenue requirement for the network. For substantial portions of the network, such as middle mile transport facilities, the network costs will be common to all services delivered over that network. Thus, the vast majority of costs fall into the common category.

While common costs can be allocated following certain accounting practices (e.g., based on the relative proportion of customers for each broad customer category), such allocations have no reliable economic basis and provide no indication of competitive market prices. Following from the example above, the relative proportions of connections across rural healthcare providers, schools and libraries, retail mass market, and enterprise customers purchasing a full range of telecommunications products plays no role in competitive markets in determining how much each customer segment should be charged for the shared and common costs of the TERRA network. Each customer segment faces different competitive options and has different demand characteristics that play a fundamental role in setting prices. The same would be true if we considered other allocation bases, such as peak demand and/or data consumed; they would produce equally meaningless results.

In summary, while FDC has provided expedient guidelines for allocating costs across customers of regulated monopolists, economists are generally skeptical that FDC-based rates are indicative of the prices that would be realized under competitive market conditions. This is due, in part, to the absence of customer demand in regulatory rate formation. Thus, using FDC as a backstop is unlikely to provide meaningful information about market prices—which appears to be the

Commission's ultimate objective. FDC-based rates cannot and do not result in efficient pricing—meaning sending the correct price signal to the market. This is particularly important when portions of the market where FDC is applied are exposed to and constrained by competitive market forces—whether present or prospective.

IV. Conclusion

We began our review with the understanding that urban and rural rates (used in implementing Universal Service support for healthcare providers) should reflect market prices to the greatest extent possible. 47 CFR § 54.603 established competitive bidding to be the primary mechanism to solicit market prices and information. As initially implemented, Sections 54.605 and 54.607 provided a regulatory backstop to make sure that prices received in the competitive bidding process accurately reflect market prices—but those indicators are also intended to provide information about prevailing market prices.

The first two fallbacks in the regulatory backstop involve compilation of prices for comparable transactions in the subject rural area. If such data is not available, the final fallback is for the telecommunications carriers to submit a cost-based rate, which would then likely become the rural rate used in determining Universal Service support. We agree that pricing information for comparable transactions would provide backstop indications of market prices, but these data can be unavailable even in the best circumstances. To address this, it should permit consideration of comparable charges for each individual rate element when there are no available end-to-end comparisons available, as market competition for each element combined with existing regulation where the Commission has retained such regulation to constrain market power will ensure that the total end-to-end rate is reasonable. In contrast, cost-based rates provide no such meaningful market information. As we discussed in greater length above, calculations of cost-based rates do not reflect market prices, regardless of how common costs are allocated. Furthermore, adding a requirement to provide cost-based rate calculations is a step much closer to an *ex ante* regulatory regime that the Commission no longer applies to non-dominant carriers and providers of the majority of business data services.

In the NPRM in WC Docket No. 17-310, the Commission also indicated that it is considering using cost-based rates as a discipline on rural healthcare providers who receive universal service support levels that the Commission finds to be particularly high, or “outliers” to more mainstream levels. We find this to be ill-advised, mainly for the reasons that we discussed above. That is, cost-based rates do little to provide efficient price signals to current and potential competitors, and also treat non-dominant providers as rate of return regulated incumbents. Furthermore, being designated an outlier likely has little to do with inefficient operations and/or mismanagement, and more to do with location, demand and marginal costs. Rates based on fully distributed costs will do little to inform efficient market prices.

We also understand that the Commission seeks assurance that the bidding process is functioning in a competitive manner. This could be productively assisted, consistent with operation of a competitive market, by facilitating the greater availability of information as to rates being

provided, such as the Commission has done with respect to its E-rate program. In addition, GCI has proposed gradual increases in the payment required of participating rural healthcare providers. Increasing payment levels would further improve the operation of market-based processes by placing a greater economic incentive on healthcare providers to make cost-effective procurement decisions, supplementing existing regulatory requirements.